Retirement Systems of Minnesota

Minnesota State Retirement System • Public Employees Retirement Association • Teachers Retirement Association

Legislative Commission on Pensions and Retirement

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Dave Bergstrom, MSRS Executive Director

Laurie Fiori Hacking, TRA Executive Director

Mary Most Vanek, PERA Executive Director

Actuarial Standards & Assumptions Need Modification

Actuarial Standards Need to Change

- Support recommendations of Legislative Auditor to change LCPR actuarial standards. Joint Retirement Boards went on record supporting this change last December.
- Market value of Post Fund assets should be on financial and actuarial reports to be GAAP/GASB compliant. Change needs to be made very soon so that FY 2007 financial and actuarial statements can be compliant.

Actuarial Assumptions Should be Updated

- Encourage LCPR to review and adopt assumption changes recommended by actuary in most recent experience studies.
- Economic and demographic assumptions such as inflation and salary increases are set in statute and need to be updated through legislation.
- The actuary retained to advise the LCPR should be invited to present these assumption changes at a hearing in the near future. LCPR should also receive a report on the actuarial status of each fund.

Retirement Plan Current Funding Status

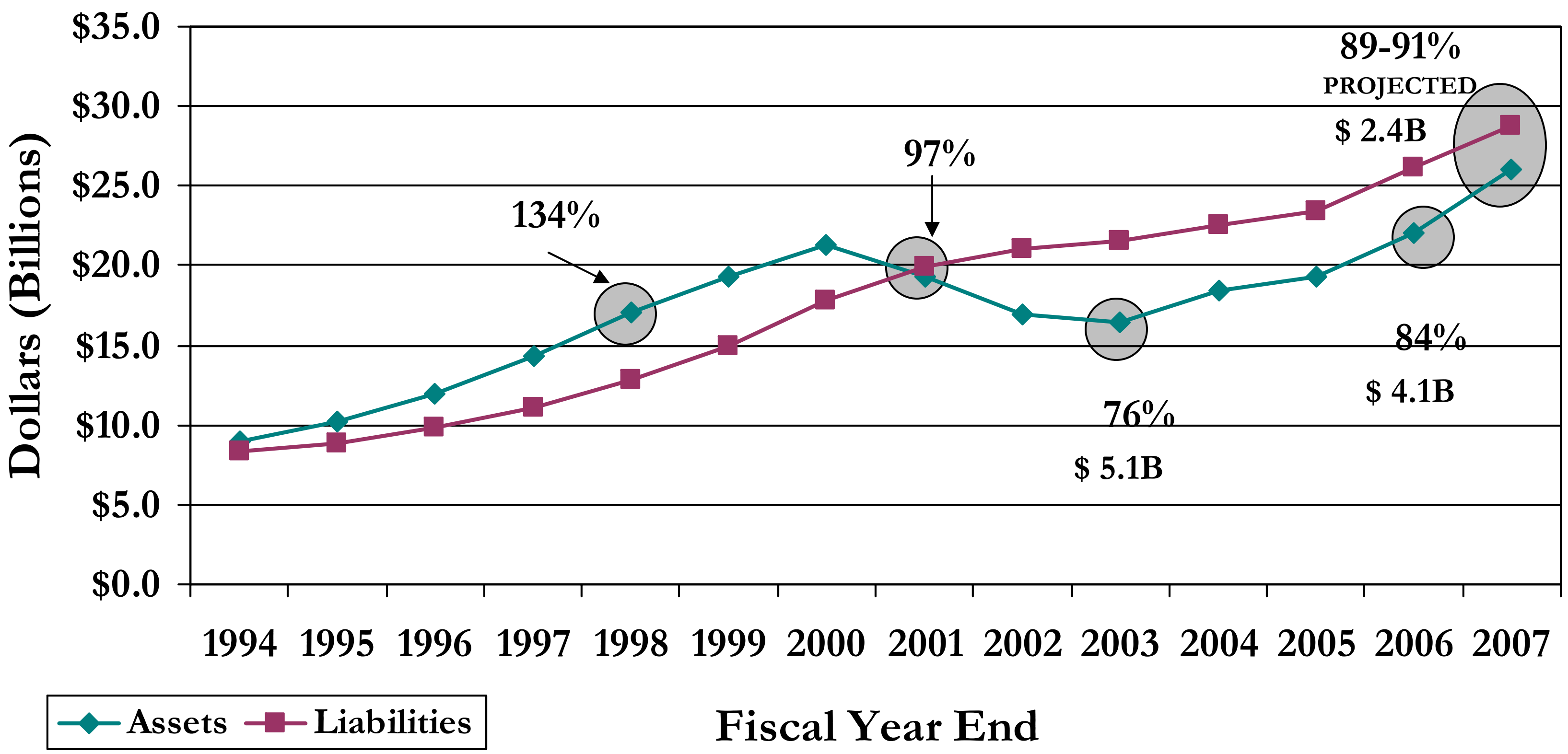
Funding Requirements for Combined Active & Post Fund

- Once LCPR actuarial standards are modified to recognize the Post Fund deficit in all funding calculations, each system's funding ratio & contribution requirements will change. Estimates are below:

Fiscal Year 2006	MSRS General	PERA General	TRA
Funding Ratio	**94.7%**	**71.9%**	**86.8%**
Total Required Contributions	9.4%	13.0%	13.5%
Contribution Sufficiency or (Deficiency)	0.6%	0.0%	(1.7%)
Calculations assume contribution increases and assumption changes fully implemented and full market value of assets recognized. Estimates based on 07/01/06 valuation data; to be updated when 07/01/07 data available.			

Sources: Mercer Consulting (MSRS and PERA analysis) & Buck Consultants (TRA).

Post Fund Funding Ratio History



Source: State Board of Investment Annual Letters to Executive Directors regarding Post Fund Benefit Increase

Joint Retirement Boards Work on Post Fund Problem

- Proposed to move from 5-year to 10-year smoothing in 1999. Not enacted.
- Proposed 5% cap on Post Fund increases in 2005. Cap enacted in 2006 (effective 2010).
- In 2006, formed Joint Post Fund Committee to develop comprehensive proposal for the 2008 session.
  - Post Fund Committee met 7 times
  - Established “Guiding Principles”
  - Informed and engaged members and stakeholder groups; reviewed hundreds of letters and heard testimony from many groups
  - Analyzed multiple reform options (10+)
  - Developed draft proposal

Summary of Post Fund Committee Principles

- Post-retirement increase mechanism should provide some form of **inflation protection** and reflect the cost of living better than the current formula.
- The increase mechanism should result in more **consistency** than the current method; **less volatility** of increases.
- The increase mechanism must be **affordable** to the plan and **financially sustainable**.
- The increase mechanism should **minimize cost** to the plan and active employees.

Joint Committee Draft Proposal

•High Investment Returns

•Deficit Reduced/Eliminated

•Sluggish/Negative Returns

•Deficit Worsens

Post Fund Continues

•Inflation Component

•Revised Investment Component (Added Inflation Protection)

•Inflation Equalizer for more recent retirees

•5% cap on increases

•Excess asset mechanism

Post Fund Sunsets

•Safeguard Merger of Post and Active Funds

•Flat 2.5% Annual cost of living (COLA)

•Additional incremental increases determined by each Plan after comprehensive benefits analysis

Joint Committee Draft Proposal

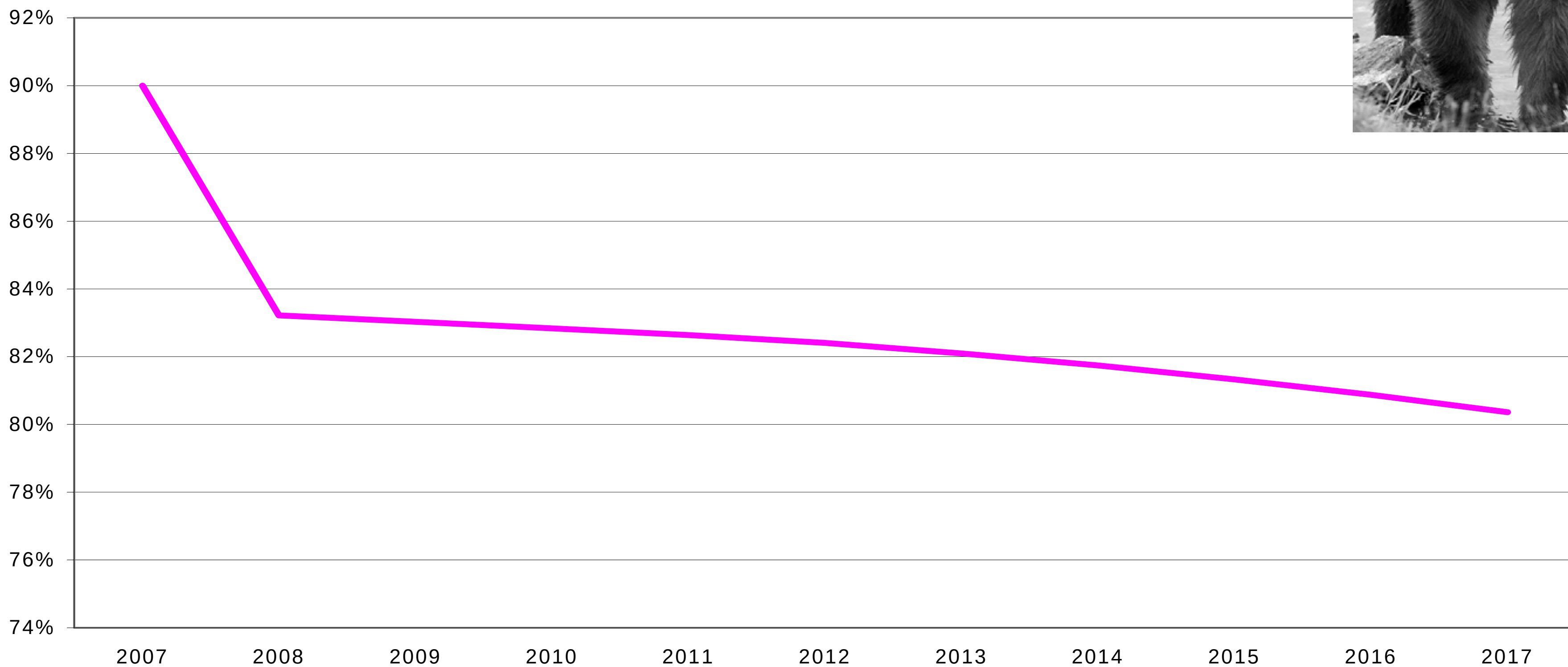
Current Law	"Draft" Proposal
Inflation Component: •100% of inflation up to 2.5%	**Inflation Component:** •Same as current law
Investment Component: •Once Post Fund is 100% funded •Additional increase paid when investment returns are high & generating excess assets •Up to 2.5%	**Added Inflation Protection:** •Once Post Fund is 100% funded •Pay added inflation increase if inflation greater than 2.5% •Up to 2.5%
5% Cap on all increases	5% Cap on all increases
	Inflation Equalizer: •If inflation is less than 2.5% •Added inflation for retirees who lag behind inflation •Paid even if not 100% funded

Important Reasons for Safeguard Merger

Action is important to avoid a worsening deficit in the Post Fund.

- The financial viability of the Post Fund is important to the financial stability of the statewide retirement funds.
  - Deficit could worsen and impact all statewide plans funding and contribution requirements.
  - Avoid a deficit that could become unmanageable.

Funding Ratio of Post Fund

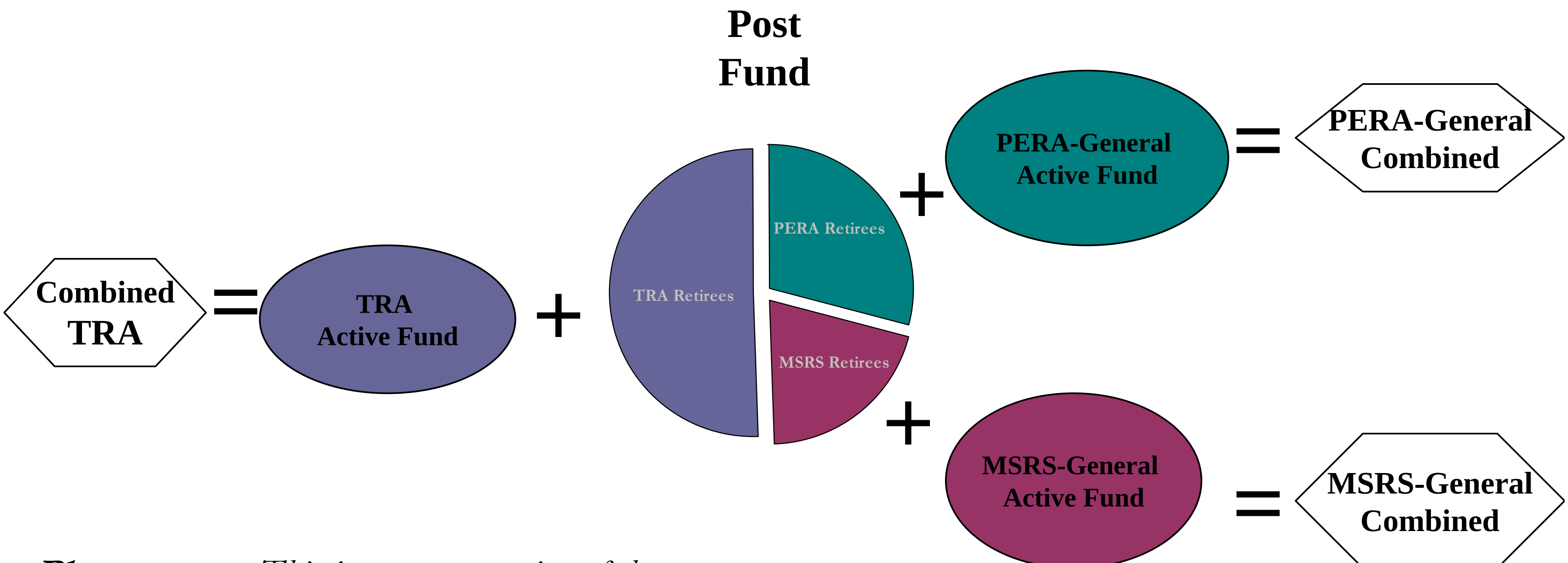


FY 08 = 0% Return
8.5% Return Thereafter

Based on:
- Participant data as of July 1, 2006
- Actuarial assumptions as of July 1, 2006
- Plan provisions as of July 1, 2006
- Stable future population
- Assumes Post Fund is 90% funded as of July 1, 2007

Analysis: Mercer Consulting

Post Fund and Active Funds Combine



Please note: *This is a representation of the General Plans for MSRS and PERA. All other plans will have separate combined funds.*

Retiree Increases if Active/Post Funds Combine

- If the Post Fund is dissolved, all retirement systems will pay a fixed 2.5% increase.
- Each board will have the opportunity to study the plans they administer and develop a proposal for Legislative action regarding how any excess assets may be shared once the plans are over 100 percent funded.

Post Fund and Active Funds Combine

- Actuarial analysis will be completed to determine some of the final details of the proposal such as:
  - A minimum funding level which will result in Post Fund structure being dissolved and Post and Active Fund for each plan combined.
  - Funding levels for dissolution of the Post Fund if reasonable progress towards full funding is not made in a reasonable time period.
- This analysis will include modeling to determine the appropriate minimum funding level to dissolve the Post Fund while minimizing the financial impact to active employees (i.e. contribution rate increases).

Next Steps to further refine the proposal

- Actuarial Analysis to determine:
  - The probability that the Post Fund will become fully funded again and a reasonable amount of time to expect recovery.
  - A mechanism to deal with excess assets if Post Fund is significantly over funded.
  - The appropriate funded ratio that the Post Fund should be dissolved if the there is a decrease in assets due to market changes. This analysis will consider the appropriate funding level to minimize contribution rate increases to active employees.
- Committee consideration of stakeholder feedback.